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BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

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JAN 15 1997

CARL J. KUNASEK
Chairman
JAMES M. IRVIN
Commissioner
RENZ D. JENNINGS
Commissioner

DOCKETED BY

IN THE MATTER OF THE COMPETITION) DOCKET NO. U-0000-94-165
IN THE PROVISION OF ELECTRIC)
SERVICES THROUGHOUT THE STATE) APPLICATION FOR REHEARING
OF ARIZONA) AND REQUEST FOR STAY

The Arizona Electric Power Cooperative, Inc. ("AEPCO"), pursuant to A.R.S. § 40-253, submits this Application For Rehearing and Request for Stay of Decision No. 59943 dated December 26, 1996 ("Application"). Rehearing and a stay pending Commission determination of the issues raised is requested as to all aspects of Decision No. 59943 and its appendices including the Rules set forth in its Appendix A (collectively, the "Decision").

I. INTRODUCTION

This Application presents a final opportunity for this Commission to alter the hastily charted course embarked upon by its predecessor concerning these issues of tremendous statewide and regional importance. In less than five months - from early August to December 26, 1996 - the previous Commission moved from an issues outline to a final Rules "framework." Along the way, it ignored constitutional provisions, statutes, well established case law, the powers of other branches and levels of government, the input of all parties to this proceeding and the procedural and substantive safeguards guaranteed participants in this process.

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1 If this Commission fails to act to alter this course, it
2 will materially retard, not advance, the common goal of moving to a
3 competitive system of electric supply which can safely, reliably and
4 economically serve the power needs of 21st Century Arizona. Instead
5 of focusing our resource on this goal, needless time and effort will
6 be expended in the court system to demonstrate the obvious - that
7 the Commission must consult with and be empowered by both the
8 Legislature and the people prior to altering the state's
9 constitutional public utility policy. Once that judgment has been
10 rendered, the entire effort must begin again thus delaying the
11 introduction of rational retail access.

12 If instead this Commission grants the Application and
13 stays enforcement of the Rules, it can reorient this process to
14 accomplish among other things the following:

- 15 ◦ Consultation with and action by the Legislature in
16 those non-ratemaking areas where it, not the
17 Commission, has jurisdiction.
- 18 ◦ Continued work by this Commission and all interested
19 parties on the myriad of unresolved and unaddressed
20 issues treated or ignored by the current version of
21 the Rules.
- 22 ◦ Coordination of this state's efforts with those of
23 other states to assure, among other things, that
24 Arizonans are not disadvantaged by a premature leap
25 to an open market while others refuse to
26

1 reciprocate. Just last month, the Western
2 Governor's Association formed a task force "to sort
3 through the complex regional issues involved in the
4 restructuring of the western electric power
5 industry."

6 ° Most importantly, consultation with Arizonans as to
7 whether and in what fashion they wish to amend their
8 Constitution to allow the Commission to regulate
9 utilities on a different basis than the one they
10 established in 1912 and have steadfastly reaffirmed
11 many times over the past eight decades.

12 The need for careful deliberation is being underlined by different
13 groups voicing different concerns. Recently, the Electric
14 Consumers' Alliance ("ECA") warned that promises of huge savings
15 from retail wheeling are inaccurate and misleading. Representing
16 more than 150 organizations speaking for consumer groups, the
17 elderly, the disabled and small business, the ECA concluded that the
18 country's largest manufacturers would benefit the most from open
19 access and the interests of small consumers are most in jeopardy.

20 In this docket, the I.B.E.W. articulated different
21 concerns in its December 20, 1996 exceptions:

22 The proposed Rule must not be implemented
23 precipitously, risking the present level of
24 industry performance.

25 * * *

1 When livelihoods, standards of living and the
2 safety of communities lay at stake, the
3 I.B.E.W. must once again voice opposition to
4 the proposed Rules as written. Although the
5 Commission staff has constructed a "framework,"
6 that is all that is in place.

7 From yet another standpoint, APS has submitted testimony which
8 estimates hundreds of millions of dollars of tax consequences for
9 the state, its schools and localities as a result of the Rules.

10 AEPCO and its member owned cooperatives have a unique role
11 in and view of this issue. On the one hand, we only exist to assure
12 a safe, reliable and economical supply of electricity for our rural
13 owners. Our customer and our stockholder are one and the same. An
14 electric bill saving is a dividend for our member owners. On the
15 other hand, we are mindful of the fact that previous competitive
16 transitions in airlines and telecommunications have in the main left
17 the rural consumer with higher cost and lower quality service - a
18 fear recognized by the Commission in its Telecommunications'
19 Universal Service Fund. Even worse, these Rules threaten the very
20 structure which has allowed cooperatives to energize rural Arizona
21 over the past sixty years and to continue to fulfill that mission in
22 the future.

23 The learned Yogi Berra once noted that "if you come to a
24 fork in a road, take it." It's good advice. Take the opportunity
25 offered by this Application and Request for Stay. Grant both and
26 proceed on a more assured course.

. . .

. . .

1 **II. THE DECISION AND RULES ARE FLAWED.**

2 The Decision is unconstitutional, unlawful, unreasonable,
3 in excess of the Commission's jurisdiction, arbitrary, capricious
4 and an abuse of the Commission's jurisdiction upon the grounds and
5 for the reasons set forth in the following documents, each of which
6 are incorporated herein by this reference as if fully set forth
7 herein:

8 1. AEPCO's letter of April 18, 1995 to Commission Staff
9 Attorney Janice Alward (a copy is attached).

10 2. The Comments of AEPCO dated June 28, 1996.

11 3. The Comments of Trico Electric Cooperative, Inc.
12 ("Trico") dated September 11, 1996.

13 4. The Comments of Arizona's Electric Cooperatives on
14 the Draft Rules dated September 12, 1996.

15 5. The Comments of the Rural Utilities Service, an
16 agency of the United States Department of Agriculture, dated
17 September 12, 1996.

18 6. The Comments of the National Rural Electric
19 Cooperative Association dated September 11, 1996.

20 7. The Comments of the National Rural Utilities
21 Cooperative Finance Corporation filed September 11, 1996.

22 8. The AEPCO, Duncan, Graham and Sulphur Springs
23 Comments on Proposed Rules dated November 8, 1996.

24 9. The Comments of Trico dated November 8, 1996.

1 10. The Comments of Arizona Public Service Company
2 ("APS") on Proposed Retail Electric Access Rules dated November 8,
3 1996.

4 11. The testimony of Messrs. Pollack, Barker, Landon and
5 Hieronymus which were attached to the APS' Supplemental and Reply
6 Comments dated November 27, 1996.

7 12. Section IV concerning legal issues, pages 22 to 34,
8 of the First Set of Comments on Proposed Rule Regarding Retail
9 Electric Competition on behalf of Tucson Electric Power Company
10 dated November 8, 1996.

11 13. The Supplemental Comments of AEPCO, Duncan, Graham
12 and Sulphur Springs dated November 25, 1996.

13 14. The Exceptions of APS to Staff's Proposed Order dated
14 December 20, 1996.

15 15. The Application for Rehearing/Reconsideration by
16 Arizona Public Service dated January 10, 1997.

17 16. The Application for Rehearing and Request for Stay of
18 Trico dated January 13, 1997.

19 In amplification of and not in limitation of the
20 foregoing, the Decision is unconstitutional, unlawful, unreasonable,
21 in excess of the Commission's jurisdiction, arbitrary, capricious
22 and an abuse of the Commission's discretion for the reasons and upon
23 the grounds set forth below:

- 24 ° The Decision violates Arizona statutes including but
25 not limited to A.R.S. § 40-281 and case law decided
26

1 thereunder by changing the public policy of this
2 state from one of regulated monopoly concerning the
3 supply of electric service.

4 ° The Decision violates Arizona's Constitution
5 including, but not limited to, its Article XV,
6 Section 6, by attempting to exercise powers
7 expressly and impliedly reserved to the Legislature
8 and the Courts.

9 ° The Decision violates Article XV of Arizona's
10 Constitution in purporting to prescribe and
11 establish rates and charges for electric services on
12 a basis other than the constitutionally mandated
13 system of a just and reasonable rate of return on
14 the fair value of the property of public service
15 corporations.

16 ° The Decision violates the supremacy clause of
17 Article VI of the United States Constitution and
18 frustrates federal law including but not limited to
19 the Rural Electrification Act of 1936, as amended,
20 by, inter alia, causing defaults on federal loans
21 and/or federally guaranteed mortgages on which AEPCO
22 and its Class A members are obligors, impairing the
23 contractual relationships between AEPCO's Class A
24 members and their member-owners and impairing the
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26

1 all requirements wholesale power contracts
2 relationship between AEPCO and its Class A members.
3 ° The Decision violates Article I, Section 10, CL. 1
4 of the United States Constitution and Article II,
5 Section 25 of the Arizona Constitution in that it
6 impairs the obligations of contracts including but
7 not limited to the contracts between AEPCO's Class A
8 members and their member-owners and the obligations
9 of contracts between AEPCO and its Class A members.
10 ° The Decision violates the just compensation
11 provisions of the Fifth Amendment to the United
12 States Constitution and Article II, Section 17 of
13 the Arizona Constitution ("just compensation
14 provisions") and the due process provisions of the
15 Fourteenth Amendment to the United States
16 Constitution and Article II, Section 4 of the
17 Arizona Constitution ("due process provisions"), by
18 breaching the regulatory compact between the State
19 of Arizona and its electric public service
20 corporations, including AEPCO and its Class A member
21 distribution cooperatives ("Class A members"), to
22 whom the Commission has issued Certificates of
23 Convenience and Necessity.
24 ° The Decision violates the due process provisions of
25 the United States and Arizona Constitutions and the
26

1 requirements of A.R.S. § 40-252 by failing to
2 provide AEPCO and its Class A member distribution
3 cooperatives with notice and an opportunity to be
4 heard prior to the amendment of their Certificates
5 of Convenience and Necessity.

- 6 ° The Decision violates the just compensation
7 provisions of the United States and Arizona
8 Constitutions by depriving AEPCO and its Class A
9 members of their vested property rights.
- 10 ° The Decision violates the just compensation
11 provisions of the United States and Arizona
12 Constitutions by confiscating AEPCO and its Class A
13 members' property for a public purpose and use.
- 14 ° The Decision violates the just compensation and
15 other provisions of the United States and Arizona
16 Constitutions by purporting to limit amounts to be
17 paid to AEPCO and its Class A members for
18 deprivation of their property rights and by assuming
19 to the Commission, not the Courts, the power of
20 determining such compensation.
- 21 ° The Decision violates the equal protection
22 provisions of the 14th Amendment to the United
23 States Constitution and Article II, Section 13 of
24 the Arizona Constitution in that it does not provide
25
26

1 equal treatment of all electric utilities and
2 electric service providers in the State of Arizona.

- 3 ◦ The Decision exceeds the Commission's statutory
4 authority to order joint use of facilities by others
5 of property owned and operated by AEPCO and its
6 Class A members.
- 7 ◦ The Decision is impermissibly vague.
- 8 ◦ The Decision impermissibly interferes with the
9 internal management and operations of AEPCO and its
10 Class A members.
- 11 ◦ The Decision exceeds the jurisdiction, power and
12 authority granted to the Commission in the Arizona
13 Constitution and the statutes of Arizona and assumes
14 powers to the Commission not granted by the
15 Constitution and statutes of the State of Arizona.
- 16 ◦ The Decision violates the requirements of the
17 Administrative Procedure Act, Title 41, Chapter 6,
18 of the Arizona Revised Statutes including but not
19 limited to the provisions of A.R.S. §§ 41-1025, 41-
20 1044 and 41-1057.

21 **III. CONCLUSION**

22 AEPCO respectfully requests that the Commission enter its
23 Order granting the Application for Rehearing and staying the
24 Decision and the Rules adopted pending resolution of the issues set
25 forth herein.

1 RESPECTFULLY SUBMITTED this 15th day of January, 1997.

2 JOHNSTON MAYNARD GRANT AND PARKER, P.L.C.

3
4 By 

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17 Original and 10 copies of the
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19 day of January, 1997, with:

20 Docket Control
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24 Copy of the foregoing hand delivered
25 this 15th day of January, 1997, to:

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April 18, 1995

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Re: **Submission of Legal Issues**
ACC Retail Electric Competition
Docket No. U-0000-94-165

Dear Ms. Alward:

In accordance with the "call for issues" discussion at the Attorney Task Force meeting held March 29, I offer the following legal issues of principal concern to AEPCO. As a rural electric cooperative, we believe these issues should be considered and resolved as part of any Commission process regarding competition and retail access in the electric utility industry in Arizona. I realize some issues may be cumulative to those raised by others on the subcommittee. However, I believe their inclusion by a number of us should heighten, rather than diminish, their importance in the Commission's decision-making process.

LEGAL ISSUES

Arizona Constitutional Issues:

1. May the ACC order or allow retail competition and not set rates, charges and classifications (e.g., through individually negotiated contracts) despite the language of Const. Art. 15, §2 and §3, which provide, in pertinent part, that the ACC "shall" prescribe just and reasonable classifications to be used and just and reasonable rates and charges to be made and collected"
2. Should IPP's, NUG's, and other corporations "engaged in furnishing electricity for light, fuel or power" be regulated by the ACC in that business as "public service corporations" pursuant to Const. Art. 15, §2 with their rates and charges, methods of operation, services, and facilities subject to such regulation, since the Commission's Constitutional power to regulate such corporations derives from a corporation's status as a public service corporation and not from any status as a regulated monopoly or as a holder of

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a CC&N.

3. Since Const. Art. 15, §3 grants the ACC exclusive and plenary jurisdiction to regulate all public service utilities within the state, "in the transaction of business within the state," does the Arizona Constitution require the ACC to regulate "retail sales" to the public within Arizona by public service corporations outside Arizona's boundaries?
4. May the ACC, through a "legislative" order (by rule-making) decide the issues of retail competition or retail wheeling, or is the ACC required by constitutional considerations of due process to decide such issues only through a full adjudicative process, giving each affected public service corporation notice and an opportunity to be heard, since any orders on this issue may require a public service corporation to alter its financing, its property, or its corporate policies in a significant manner?
5. Case law holds that the ACC is under a duty to protect a public service corporation in its exclusive right to serve electricity in the area where it renders service under its certificate. Further, the ACC is under a duty to prohibit other utilities under its jurisdiction from competing in such arena unless, after notice and opportunity to be heard, the Commission finds that the public service corporation failed or refused to render satisfactory and adequate service at reasonable rates. Therefore, once the ACC has issued a CC&N, may it rescind, alter, or amend it by ordering retail competition?
6. If compensation should be paid for the "taking" of a CC&N as a vested right, what is the proper measure of compensation: the utility's profits, its margins, its earnings, the expenses covered by the load lost; the resulting rate increases to members or ratepayers from the loss of the monopoly load?
7. Since the power of the ACC lies in whether a utility is a public service corporation, and not whether the public service corporation is subject to a CC&N, and the Arizona Constitution prohibits discrimination by a public service corporation in charges, services, and facilities, does the ACC have the authority to order retail wheeling with the discrimination that is inherent to retail competition?

Electric Cooperative Issues:

1. Will the Rural Utilities Service (RUS), successor in interest to the REA, as a creditor agency and regulator, preempt ACC-ordered retail wheeling which adversely affects RUS borrowers in order to protect its rights as a mortgage holder?
2. Will the RUS preempt ACC-ordered retail wheeling because the state action would

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frustrate the federal purpose of the Rural Electrification Act (RE Act) to provide reliable and economically priced electric service to as much of rural America as economically feasible? Note that a purpose of the RE Act was also to end abuses by private utility companies, particularly the cream skimming of customers that had prevented the full electrification of rural America, and to maximize rural electrification by using more profitable areas and customers to leverage less profitable ones to "avoid the stranding of considerable areas which cannot be self sustaining....."

3. Cooperatives cannot dispose of property without RUS approval; nor can non-RE Act beneficiaries use the property of Act beneficiaries. 7 USC §907 would prohibit the disposal of franchises, property or rights that are assets, including exclusive service territories.
4. Most cooperatives are IRC Section 501(c)(12) tax exempt entities because their member income is at least 85% of total income. Revenues from non-members likely would increase with ACC-ordered retail wheeling. Will this cause cooperatives to lose their tax exempt status as a non-profit corporation in order to follow ACC orders? Will Arizona's cooperative enabling legislation provide that a transmission-only customer can be a member? Will the IRS accept this rather loose member policy or find it a sham?
5. The All Requirements Contracts inherent to G&T and Distribution cooperatives establish a unique set of legal rights and obligations since they secure RUS loans and effectuate RUS policy to provide the economic means to supply electricity to rural areas; they provide a revenue stream corresponding with the G&T's repayment of its debt obligation and these contracts cannot be avoided nor abrogated by state action.
6. Electric cooperative systems built with RUS funds can only be used to serve RE Act beneficiaries. Can RE Act funded existing systems serve non-member loads? ACC imposed retail wheeling may put the cooperatives in the position of being unable to obtain RUS financing for system additions needed for retail wheeling if the wheeling is considered non-Act beneficiary load. Additionally, will the RUS finance system additions to serve load that is retail load a member has obtained from another supplier?
7. What happens with a customer who leaves and then returns, if the ACC requires utilities to serve customers who have departed but wish to reconnect. Would that customer be an Act beneficiary?
8. Will the RUS consider retail loads "won" by a cooperative away from another supplier to be Act beneficiary load?
9. Pricing considerations in any retail wheeling program need to address the unique

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characteristics of the G&T/distribution cooperative structure as to pricing (This may, in all likelihood, also be a FERC matter as to the G&T).

10. If the distribution cooperatives were regulated by the ACC, but the G&T were non-regulated or regulated by FERC, can the ACC create a pricing policy that does not trap costs that cannot be recovered. Note that with no shareholders, the Government and other lenders are left bearing unrecovered costs.
11. Given the capital structure of cooperatives, it is unclear what a fair pricing policy for non-member transmission service would be. Should non-Act beneficiaries get the benefit of assets purchased with low interest government loans? The ACC should take into consideration the current subsidy a cooperative obtains through the RUS for RE Act beneficiary purposes. A non-RE Act beneficiary should not benefit to the detriment of the RUS borrowers. For example, if an RUS borrower is ordered to expand its system, and the rate charged to the non-RE Act beneficiary is based on the RUS borrower's embedded cost of debt, the non RE Act beneficiary would get the benefit of the loan subsidies through the borrower's weighted average cost of debt in the computation of rates and the RE-Act beneficiary costs would increase. Additionally, should there be an assumed return on equity in pricing that emulates what shareholders would receive that would go to enhance member equity?
12. How will stranded generation costs be handled? If the solution is based on an assumption of integrated electric systems, is there a possibility of inconsistent state/federal regulatory schemes that trap costs for non-integrated cooperative systems?
13. RUS must approve any transmission service agreement entered into by a G&T or distribution cooperative. May and will RUS use that approval to preempt ACC regulatory action mandating retail wheeling? Must and will it do so on a case-specific base, as it has with annexation, rather than generically?
14. RUS must approve a cooperative's rates for transmission service and for power sales. Exit fees, generic adders, and other devices to recover or not recover full stranded costs are thus subject to RUS review. May and will RUS use its review power to preempt ACC action? Will RUS develop a general guideline as to the rate structures it finds adequate to protect RUS security? Alternatively, will RUS merely review rates on a case-by-case basis as it now does power sales?
15. Will RUS urge FERC to take over all pricing for wheeling, deciding that it would be far better off having FERC determine pricing to the extent possible, rather than having to track numerous state proceedings?
16. Is retail competition inherently discriminatory to the isolated rural customers who lack

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Janice Alward, Esq.

April 18, 1995

Page 5

sufficient density to benefit from any direct access plans and whose transaction costs are too high? Private utility companies' historic records with rural customers led to the formation of rural electric cooperatives -- the original concept of direct access. Note that in every deregulated market (gas, airlines, telephone) costs are higher to the isolated and the inelastic customers.

17. The Cooperative system has a unique structure as a unified system; it is not an integrated utility. A G&T cooperative is owned by the distribution cooperatives to provide them with economically priced power. It would be unable to provide that cost-effective service if the system were dismantled piecemeal.
18. If the ACC were to continue to protect CC&N's for distribution and order retail competition only for generation, does this discriminate against the state's only regulated generation and transmission (G&T) utility, since all other utilities with both generation and distribution would continue to hold their vested rights to a CC&N? Is there any legitimate policy basis for sheltering from the adverse consequences of competitive markets only those who own distribution while denying protection to one equally at risk, but which lacks the structure to own distribution facilities?
19. Stranded investment cost recovery cannot ever resolve the problems which resulted in the service territory concept: duplication of facilities with resulting financial and environmental consequences; cream-skimming where the "best" loads are taken, leaving the poor load factor and less dense areas for the cooperatives; the creation of death spirals, as rates to remaining customers escalate when the most profitable loads are taken; the loss of loads which would place RUS loans at risk, and shift a RUS cooperative's property, its CC&N rights, to the benefit of a private entity for that entity's gain at the expense of the government.

Other Legal Issues:

1. Do we really want to transfer Arizona's regulatory playing field to Washington, D.C.? If the ACC orders retail wheeling, will FERC, in effect, replace the ACC as Arizona's utility regulator since transmission lines, coordination services, regional power pools, and wholesale sales are all interstate commerce, and, by and large, already FERC regulated? If the ACC authorizes retail wheeling; does FERC automatically take over; will there be an inadvertent abdication of ACC regulatory responsibility?
2. The ACC does not regulate municipalities yet if it orders retail wheeling the municipalities could sell their power and wheel it over the regulated utilities' lines to the regulated utilities' former customers. However, the ACC could not require reciprocity by the municipalities. Cities could "cherry pick" or "cream skin" from a regulated utility at will, and keep the municipalities' customers "hands-off" from the regulated

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utilities.

3. Is compulsory non-consensual retail wheeling an unlawful confiscation of a utility's property in violation of the due process and equal protection provisions of the 14th Amendment?
4. If the ACC allows recognition of stranded investment and facilitates the recovery of stranded investment-related charges by any public utility, should it not also require, as a condition precedent to the eligibility for such recovery, a commitment that the public utility and any of its affiliates will compensate any other utility that they subject to stranded investment costs?
5. Where is the dividing line between states and federal jurisdiction over these issues? Can transportation jurisdictions realistically be allocated along retail/wholesale lines?
6. If the ACC decides to forego unregulated retail wheeling, can mechanisms be put in place to prohibit "retail" customers from transforming themselves into "wholesale" customers to avoid paying for the cost of plant and facilities prudently incurred under the utilities' obligation to serve?
7. If retail competition becomes a reality, what happens to future customers' needs? Who will plan for them? In a true competitive market, all will build according to short-term needs and economic standards: no one will build to meet long term needs which might be more expensive; market pressure will control; forget about reliability over the long term; forget about reasonable cost to those left behind. If this is a likely result, is there still a need for the regulatory compact to keep rate payers from becoming unwilling equity partners of the dealers in the new wholesale/retail competitive marketplace?
8. Would compulsory retail wheeling impair the obligations of the public service corporation's franchises, their joint electric coordination agreements, joint economic dispatch, and the interconnection contracts with neighboring utilities and cities which provide emergency power and short-term sales.
9. Can a form of the telephone universal service fund be implemented to mitigate the impact of retail competition to similar "high cost" service areas?

Solutions Other Than Mandated Retail Wheeling:

1. Require efficient interchange of energy and capacity among utilities to assure the efficient use of existing utilities.
2. Allow utilities, under the current ACC regulatory system, to freely negotiate contracts

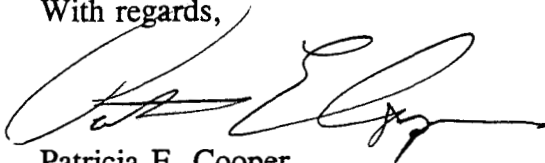
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Janice Alward, Esq.
April 18, 1995
Page 7

with their Certificated area customers at rates sufficient to cover utility costs. At the same time, provide tariffs for those customers unwilling or uninterested in negotiating individual contracts with their certificated utility. Hold utilities accountable for contract "losses," while providing flexibility to prevent potential loss of load to unregulated entities, other states' utilities, or municipalities. This is a viable alternative to a state mandated retail wheeling system that retains distribution service areas and tariffs. Such a system can result in regulated utilities being required to charge tariffed rates while other power suppliers can offer the same customers lower, unregulated, retail wheeled rates.

These are the legal issues which come readily to mind. As well, AEPCO concurs with Steven Wheeler that the issues raised by Arizona Public Service must also be considered and resolved. AEPCO looks forward to continued participation in this process.

With regards,



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